

Aqua America, Inc.

WTR: EPS Outlook Updated As ALJ Recommends Approval Of Peoples Acquisition

Market Perform/\$46

Water Utilities
Market Weight

Earnings Estimate Revised Down

- EPS Outlook Updated As Peoples Merger Close Timing Comes Into Focus.** The assigned Administrative Law Judge (ALJ) to the Peoples merger docket issued the long awaited recommended decision (RD) on 10/28. ALJ Long's RD not only approves WTR's acquisition of the Peoples Companies but adopts the non-unanimous settlement agreement in its entirety. This includes the proposed \$120M investment over a 7-year period to update the deteriorated 1,700 customer, 368 mile Goodwin and Tombaugh (G&T) gathering system and replace the existing bare steel pipe as well as a one-time \$13M rate credit offered by WTR to partially offset this cost. WTR and the seven other settling parties, including key intervenor Office of Consumer Advocate (OCA), support updating the G&T system as the preferred path forward and socializing those costs across Peoples entire customer base whereas the PaPUC's Bureau of Investigation & Enforcement (I&E) and Office of Small Business Advocate believe those customers that cannot be updated economically should be abandoned and forced to convert to an alternative energy source. In fact, ALJ Long goes as far as to characterize the remediation of the G&T system as the most significant benefit of the transaction.

As we previously discussed, parties have 30 days from the RD to file exceptions and it is likely that the PaPUC (Pennsylvania Public Utilities Commission) may take at least 30 days after that to render a final decision (absent the parties reaching unanimous settlement in light of the ALJ's RD). As such, WTR now anticipates a December 2019 or early 2020 close. We are encouraged by the ALJ's RD and anticipate the PaPUC is likely to ultimately adopt the RD.

We lower our 19E EPS to \$1.19 from \$1.32 to reflect an assumed YE'19 close by removing the roughly two months of Peoples net income benefit from our previously assumed end of October '19 deal close. In addition, we made a few other tweaks to our model, primarily related to external financing assumptions including correcting an error that overstated some cash inflows in 2019. As a result, we adjust our 2020-23E EPS down modestly to/from \$1.57/\$1.58, \$1.70/\$1.71, \$1.80/\$1.82 & \$1.92/\$1.94. This results in a 6.5-7.0% EPS CAGR. As a reminder, our outlook continues to exclude any potential uplift from the planned election of repairs tax deduction at Peoples in 2020. We reiterate our Market Perform rating but lower our 12-18 month price target to \$46/share from \$47 to reflect lower peer multiples since our last update.

	2018A	2019E	2020E
\$ EPS		Curr. Prior	Curr. Prior
Q1 (Mar.)	0.29	0.28 A	NC NE
Q2 (June)	0.37	0.35 A	NC NE
Q3 (Sep.)	0.44	0.39	0.40 NE
Q4 (Dec.)	0.31	0.19	0.30 NE
FY	1.41	1.19	1.32 1.57 1.58
CY	1.41	1.19	1.57
FY P/EPS	31.8x	37.7x	28.6x
Rev.(MM)	838	895	1,979

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
 NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
 V = Volatile
 WTR's 2019 ongoing diluted EPS guidance of \$1.45-1.50 excludes ALL Peoples related impacts. Our estimates are pro-forma Peoples, ex costs to complete.

Ticker	WTR
Price Target/Prior:	\$46/\$47
Price (10/28/2019)	\$44.90
52-Week Range:	\$32-47
Shares Outstanding: (MM)	215.7
Market Cap.: (MM)	\$9,684.9
S&P 500:	3,022.55
Avg. Daily Vol.:	1,029,020
Dividend/Yield:	\$0.94/2.1%
LT Debt: (MM)	\$2,749.0
LT Debt/Total Cap.:	40.4%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	7.0%
CY 2019 Est. P/EPS-to-Growth:	5.4x
Last Reporting Date:	08/06/2019 After Close

NC = No Change

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 3 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 10/29/19 unless otherwise stated. 10/29/19 00:01:53 ET

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Together we'll go far



Price Target

Price Target: \$46 from \$47

Our \$46/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 2.5% discount to our 70% water/30% gas utility hybrid multiple to our 2021E of \$1.71. The 2.5% discount reflects merger execution/integration risk. For WTR's water utility multiple, we start with AWK's 2020 P/E multiple of 30.3X (AWK represents the closest publicly traded peer) and apply a 5% discount (given AWK's higher growth rate and best-in-class management team). For WTR's gas utility multiple, we utilize the 2020 pure play gas LDC median of 24.6X. Key risks include regulatory and M&A strategy execution related.

Investment Thesis

We are attracted to WTR's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Market Perform rating reflects valuation considerations in light of WTR's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

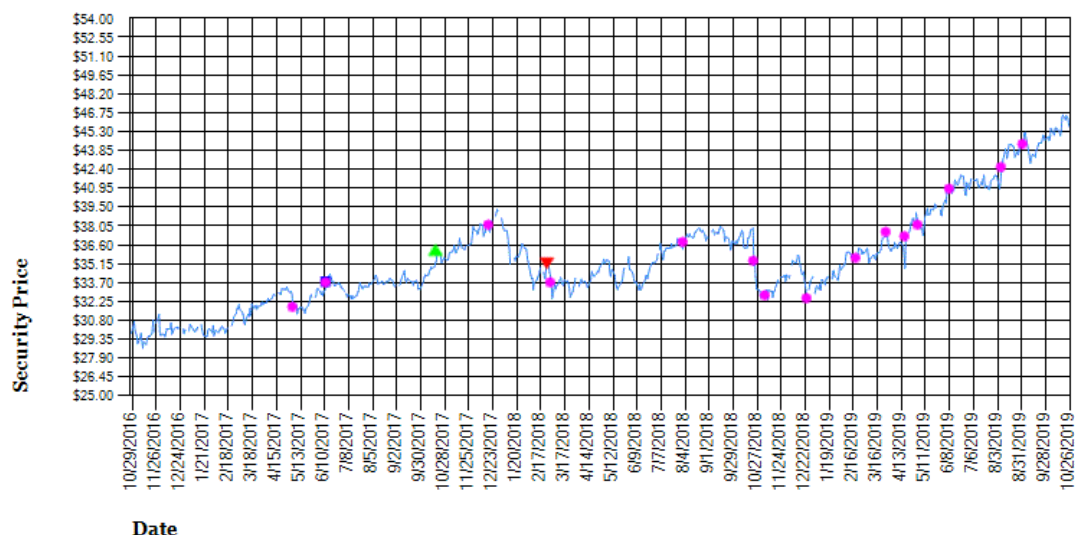
Company Description

Headquartered in Bryn Mawr, PA, Aqua America (WTR) is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTR's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total customer base and nearly 70% of consolidated rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio. Regulated operations account for more than 99% of consolidated revenues.

On 10/23/18, WTR announced a deal to acquire Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of \$4.275B (includes \$1.3B of assumed debt). From a price perspective, the deal appears to be 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to what we have seen in recent gas utility transactions. WTR expects to close the deal around YE'19, subject to receiving the final necessary regulatory approval from PA. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Required Disclosures

Aqua America, Inc. (WTR) 3-yr. Price Performance



Date	Published Price (\$)	Rating Code	Price Target	Val. Rng. Low	Val. Rng. High	Close Price (\$)
10/26/2016		Kalton				
10/26/2016	NA	2	NE	31.00	33.00	29.86
5/4/2017	31.70	2	NE	32.00	34.00	31.73
6/13/2017		Reeder				
6/13/2017	33.62	2	35	NE	NE	33.62
10/19/2017	35.30	1	40	NE	NE	36.03
12/18/2017	38.14	1	43	NE	NE	38.03
2/25/2018	35.00	2	37	NE	NE	35.00
3/1/2018	34.19	2	36	NE	NE	33.66
8/2/2018	36.70	2	38	NE	NE	36.70
10/24/2018	35.01	2	37	NE	NE	35.29
11/6/2018	32.70	2	35	NE	NE	32.59
12/24/2018	33.87	2	34	NE	NE	32.38
2/19/2019	35.54	2	36	NE	NE	35.52
3/26/2019	37.52	2	39	NE	NE	37.52
4/18/2019	36.52	2	38	NE	NE	37.15
5/3/2019	37.85	2	39	NE	NE	38.09
6/9/2019	40.84	2	42	NE	NE	40.84
8/8/2019	42.06	2	44	NE	NE	42.47
9/2/2019	44.29	2	47	NE	NE	44.29

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

Rating Downgrade

Rating Upgrade

Price Target/Val Range Change

Initiation, Resumption, Drop or Suspend

Analyst Change

Split Adjustment

Rating Code Key

1 Outperform/Buy

2 Market Perform/Hold

3 Underperform/Sell

SR Suspended

NR Not Rated

NE No Estimate

Additional Information Available Upon Request

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WTR: Key risks include regulatory and M&A strategy execution related.

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3=Underperform: The stock appears overvalued, and we believe the stock's total return will be below the market over the next 12 months. SELL

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M=Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.

U=Underweight: Industry expected to underperform the relevant broad market benchmark over the next 12 months.

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V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: October 29, 2019

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